

VZCZCXRO6151  
RR RUEHRG  
DE RUEHSO #1002/01 2611336  
ZNR UUUUU ZZH  
R 181336Z SEP 06  
FM AMCONSUL SAO PAULO  
TO RUEHC/SECSTATE WASHDC 5774  
INFO RUEHBR/AMEMBASSY BRASILIA 6833  
RUEHRG/AMCONSUL RECIFE 3137  
RUEHRI/AMCONSUL RIO DE JANEIRO 7434  
RUEHAC/AMEMBASSY ASUNCION 2772  
RUEHBU/AMEMBASSY BUENOS AIRES 2458  
RUEHLP/AMEMBASSY LA PAZ 3025  
RUEHRC/DEPT OF AGRICULTURE WASHDC  
RUEAWJC/DEPT OF JUSTICE WASHDC  
RUEAIIA/CIA WASHDC  
RHEHNSC/NSC WASHDC  
RHMFISS/CDR USSOUTHCOM MIAMI FL

UNCLAS SECTION 01 OF 04 SAO PAULO 001002

SIPDIS

SENSITIVE  
SIPDIS

STATE FOR WHA/BSC  
NSC FOR FEARS  
SOUTHCOM ALSO FOR POLAD

E.O. 12958: N/A

TAGS: [PGOV](#) [PREL](#) [EAGR](#) [ETRD](#) [ENRG](#) [SENV](#) [KPAO](#) [EINV](#) [ECON](#) [BR](#)

SUBJECT: SOUTHWEST BRAZIL: CATTLE CRISIS, POROUS BORDER, AND U.S.  
INVESTMENT IN PAPER

-----  
SUMMARY  
-----

11. (SBU) Consul General (CG) recently visited Brazil's southwestern border state of Mato Grosso do Sul. Meetings with representatives of the cattle ranching sector and government researchers shed light on an economic dichotomy in the Brazilian beef industry today: Drought conditions, market worries regarding Foot and Mouth Disease, and a general lack of business credit fuel an ongoing crisis in Brazil's cattle ranching sector, while Brazilian slaughterhouses are experiencing business growth due to expanding export opportunities and the relative strength of the Brazilian currency. Because cattle ranchers are not seeing the profit margins enjoyed by meat packers, more and more ranch owners are converting pasture land into sugar cane fields in an effort to cash in on Brazil's new hot commodity -- ethanol produced from cane. At the same time, on the eastern edge of the state, U.S.-based International Paper Corporation is poised to break ground on a new, billion-dollar pulp and paper processing plant to capitalize on 20 years of land purchases and tree farming. Meanwhile, state government leaders talk frankly of the challenges they face policing a long and porous border with Bolivia and Paraguay, and of how their state is used as a "contraband corridor" to the rest of Brazil. The CG gave a number of interviews to local TV and print media, and participated in a public diplomacy event that highlighted Mission investments in local educational projects.  
END SUMMARY.

-----  
WATER, WATER NOWHERE; NOR LOANS, NOR FMD RELIEF  
-----

12. (SBU) A visitor to Mato Grosso do Sul is immediately struck by the wide open, expansive terrain that has fostered huge cattle ranches, many of which have been passed down from colonial titles. Individual ranchers raise as many as 20,000 head of cattle at a time, and the landscape is dotted with the distinctive white-gray Brahman breeds imported from India in the 19th Century to withstand the heat and relatively dry conditions. While in the state, the CG met researchers and outreach specialists at a center near the state capital of Campo Grande, run by the federal government's agricultural research enterprise, Embrapa. He also toured a large

family-owned cattle ranch and had lunch with members of the Federated Industries of Mato Grosso do Sul (FIEMS), many of whom own businesses related to cattle ranching. The common theme struck by all participants in these meetings was that the cattle industry in this part of Brazil is in a state of crisis. A lingering drought has driven up operating costs, and because of Brazil's notoriously high interest rates, ranchers say they are hard pressed to obtain favorable commercial bank loans or lines of credit. Furthermore, the price local ranchers receive for exports of their product -- live cattle -- has been stunted by the relatively appreciated value of the Brazilian Real and a constricted world market for Brazilian beef caused by an outbreak of Foot and Mouth Disease in 2005.

13. (SBU) Cattle ranchers in Mato Grosso do Sul are still reeling from the 2005 outbreak of Foot and Mouth Disease (FMD), known regionally as Aftosa Fever. As a result of the outbreak, some 34,000 head of cattle were destroyed, and 50 countries banned the import of beef from certain regions of Brazil, which is the world's leading exporter of beef. The bans have been lifted gradually for products from the state and from the neighboring states of Parana and Sao Paulo, but new cases were reported in Mato Grosso do Sul in August of this year. Cattle ranchers decry the embargos, claiming they suffer unfairly because their industry is more transparent than those in neighboring countries; international control of FMD is based largely on self-reporting of cases. Brazilian cattle ranchers insist that their competitors in Paraguay, for example, are not affected by bans because their animals are not tested as a matter of routine, and thus, no negative report is ever generated that would trigger international embargos. Highlighting this cross-border dispute, in August 2006 Paraguayan officials announced the destruction of 16 bulls suffering from what the Paraguayans called a bacterial infection and not the Aftosa viral infection. Mato Grosso do Sul officials were skeptical of the diagnosis, and threatened to close some 250 miles of the state's border with Paraguay. (NOTE:

SAO PAULO 00001002 002 OF 004

The United States periodically imposes various limitations on the importation of Paraguayan and Brazilian beef products. END NOTE.)

-----  
FROM COW PIES TO GASOLINE  
-----

14. (SBU) Ranchers and state government officials noted that a growing number of landowners are converting pasture land to sugar cane in order to capitalize on the ethanol craze that is sweeping the energy and agriculture sectors of Brazil and much of the world. Government officials said that several large-scale and famous American investors have expressed interest in acquiring property and facilities in Mato Grosso do Sul for sugar and ethanol production. In the near to mid-term, any such significant conversion of pastureland to sugar cane should have little impact on the overall level of beef production, since currently Brazilian cattle enjoy the largest grazing acre-to-cow ratio in the world.

-----  
WHILE BRAZIL'S MEAT PACKERS PROSPER  
-----

15. (U) Despite the widely discussed "cattle crisis," Brazil remains the world's leading beef exporter, and exporters here achieved record sales in the first half of 2006. From January to July, Brazilian beef exports totaled \$2 billion, a 15.5 percent increase over the same period last year. Even though it only recently lifted its official ban on Brazilian beef, Russia remained the largest single importer of Brazilian raw cattle products, while the United States was the largest importer of processed beef products. A surge in exports to Arab nations, particularly Egypt, helped minimize the effects on meat packers' profits of the 50-nation embargo on Brazilian beef due to the Aftosa scare and the relatively high value of the Real on international foreign exchange markets.

16. (U) Brazil currently exports 31% of the beef sold on world markets, and two new giant slaughterhouses may increase the country's market share even further in the coming year. The Frioli Group plans a new plant in Rio Grande do Sul that will process 1,000

head of cattle per day with room to expand to 2,000, and the Bertini Group announced that it is investing \$100 million to build the world's second largest slaughterhouse in Mato Grosso do Sul. The Bertini plant, due to be completed in May 2007, will have the capacity to slaughter 3,000 head of cattle per day. But at the same time, cattle prices have fallen and producers' operational costs have risen, highlighting the almost polar economic positions of Brazil's cattle ranchers and of its meat packers, particularly exporters.

-----  
WHERE THE EUCALYPTUS GROWS FAST  
-----

¶7. (SBU) The CG visited the forestry operation of U.S.-based International Paper Corporation near Tres Lagoas on the far eastern edge of Mato Grosso do Sul, where it borders Sao Paulo State. Since the late 1980s, International Paper has been steadily buying contiguous parcels of land or establishing production agreements with land owners, and planting large tracts of commercial eucalyptus trees. Company representatives said that, due to unique aspects of the region's climate, soil characteristics and biodiversity, eucalyptus trees grow particularly quickly for pulp production there, reaching peak maturity in seven years. The company's forestry manager showed the nursery facilities, where tree cuttings are cared for until they sprout roots and are eventually planted in rows, plantation style. A variety of saplings are first planted in a test plot on each land parcel so foresters can determine which of the test trees will grow to the best specifications for the company's pulp needs. They then take cuttings from the best tree to produce others identical to it: this process is continued to fill the entire parcel with clones of the original tree. The company thus maximizes each parcel of land by cultivating trees uniquely suited to its specific and localized conditions.

¶8. (U) The company has also taken steps to preserve tracks of wild  
SAO PAULO 00001002 003 OF 004

forests and wetlands. By federal and state law, landowners must set aside a percentage of each parcel of land purchased for commercial use to be kept in a "natural" state. In a unique project, International Paper has linked a series of natural forest areas among its various land holdings around Tres Lagoas to create a contiguous forest corridor larger and potentially more environmentally sound than the individual set-asides required by law. This corridor not only provides a continuous range of natural trees and coexisting biodiversity, instead of a patchwork of smaller stands of trees, it also creates a greater buffer zone along area wetlands.

¶9. (SBU) International Paper has been planning to build a major pulp and paper mill in the Tres Lagoas area for many years, but economic and market considerations stalled the project several times. The company now seems fully prepared to start construction on what it says will be a \$1.5 billion investment in a state-of-the-art pulp and paper mill, but it also has been seeking out partners for the venture. We were told that most environmental and other governmental permit hurdles -- Brazil is notorious for bureaucratic quagmires associated with the start-up and closing of businesses -- have been overcome, and the company expects final clearance to break ground by the end of October. Construction may require as many as 10,000 temporary workers building the component "islands" of the plant simultaneously, rather than having a single contractor build the facility from the ground up. The design engineer explained that the plant will utilize leading technologies and design features, including waste recovery that will be used to generate power. In fact, once started, the plant should become energy self-sufficient, and will actually add power to Brazil's grid for which the company will receive payments or credits.

-----  
YOUTH AMBASSADORS AND INDIGENOUS FILM PROJECT  
-----

¶10. (U) In addition to giving a number of interviews to local TV and print media, the CG also participated in a public affairs

outreach event with the Mato Grosso do Sul Secretary of Education. This event took place at a local high school and was attended by a cross section of state educators, policy makers, parents and students. The event highlighted several Mission-supported projects. The CG awarded a certificate of participation to a young man from a largely rural area of the state who had participated in the Mission's Youth Ambassadors Program. He was chosen as one of only 25 participants out of 2000 applicants to spend two weeks in the United States both meeting official representatives and staying with a host family and attending the local public high school.

¶11. (U) The CG also awarded a certificate to a principal who participated in a Mission-sponsored exchange program and acknowledged the Mission's book donation to the principal's school. The event, which included an indigenous dance performance from several ethnic groups in the state, also highlighted a documentary film currently in production that the Mission has supported financially. When completed in the coming months, the film will chronicle the various indigenous "Indian" groups of Mato Grosso do Sul that still maintain a discreet identity and live in reservation-like settings. In recent years many of these indigenous groups have faced severe poverty and even food shortages, and have been involved in sometimes violent confrontations with neighboring land owners trying to displace them, and with government agents whom the groups allege act unjustly or with little effect. The State Secretary of Education will show the film to public school children

SIPDIS

in Mato Grosso do Sul to promote awareness and understanding of this aspect of their society.

-----  
LONG ON BORDER, SHORT ON CAPACITY TO CONTROL IT  
-----

¶12. (SBU) Mato Grosso do Sul Governor Jose Orcirio Miranda dos Santos (known as "Zeca do PT" for his party affiliation), Secretary of Public Security Raufi Antonio Jaccoud Marques, and various police commanders told the Consul General of the difficulty they face

SAO PAULO 00001002 004 OF 004

monitoring the long border that the state shares with both Bolivia and Paraguay. As an international border, federal agencies from each country maintain ultimate control of the border itself, but a lack of capacity and will, particularly on the Bolivian and Paraguayan sides, according to these officials, leaves the state vulnerable to criminals who use the porous border as a means to smuggle drugs and contraband into Brazil. Security officials described the state as a "corridor" for contraband, with most of the smuggled products passed onward to the more populous areas of southern and central Brazil. In addition to Bolivia and Paraguay, Mato Grosso do Sul also shares borders with five Brazilian states, including Sao Paulo and Minas Gerais.

¶13. (SBU) Police officials openly discussed their challenges, including the prevention of poaching of highly regarded wildlife along the state's northwestern edge, a flat, marshy wilderness area called the Pantanal. One police commander specifically requested USG help in coordinating efforts between Brazil, Paraguay and Bolivia regarding animal protection, noting "the animals do not stop at the border," but environmental protection enforcement often does.

The CG has discussed this with CONGEN and Embassy law enforcement representatives and with USAID officers, who will follow up to explore possible regional seminar or information exchange opportunities.

-----  
COMMENT: DEALING WITH CHANGE  
-----

¶14. (SBU) Steady rainfall will help the region of southwestern Brazil with some of its agricultural and environmental challenges. (NOTE: The water level at the massive Iguazu Falls in nearby Parana State was at 20 percent of normal during the early July visit of CODEL CORNYN, and forest fires in the nearby national park were

sparked in the unusually dry conditions. END NOTE) However, the state is also facing some transitional conditions that will bring a boom to some, and possibly a bust to others. The beef industry continues to face economic conditions creating a dichotomy between cattle ranchers, who have been bearing the cost of unfavorable conditions like weather, disease and currency exchange rates, and the slaughterhouses, who have managed to buffer and even prosper in the same economic environment by reducing payments to ranchers while exploiting new international markets. Almost everyone in the state seems to have some connection to raising cattle; even some politicians we encountered who do not depend on ranching for a living maintain small "hobby ranches" with a few hundred head of cattle. But unless the ranchers can pry loose some investment capital or make gains on the price of their cows, the economic dichotomy and their "crisis" will continue.

¶15. (SBU) Investments in sugar cane and alternative crops like pulp wood may help turn around the fortunes of landowners, suppliers and service industries, but there are concerns that the influx of temporary and seasonal labor needed for these enterprises will overwhelm small communities once the work wraps up.

¶16. (SBU) Many in government tout the economic potential of the state's natural beauty and wildlife that are famous among eco-tourists but remain relatively untapped as sources of tourism dollars. Increasingly, tighter enforcement at Brazil's major ports and border crossings has pushed contraband runners to use wide-open, untamed and largely unmanned territories like Mato Grosso do Sul as crossing points and corridors to their main markets of Sao Paulo, Belo Horizonte, Rio de Janeiro and beyond. If local, state and federal government officials want to better develop the area for tourism, security will have to be assured, and will need to be managed better than in Brazil's current slate of destination cities. Campo Grande is a surprisingly modern, well-developed and enjoyable city lying at the gateway to tremendous natural beauty and economic opportunity. How these assets are tapped and managed will dictate the state's future. END COMMENT.

¶17. (U) This cable was coordinated/cleared by Embassy Brasilia.

MCMCULLEN